

VETERANS MEMORIAL HOSPITAL
WAUKON, IOWA

FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

VETERANS MEMORIAL HOSPITAL

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VETERANS MEMORIAL HOSPITAL

OFFICIALS

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
<u>Board of Trustees</u>		
Dennis Lyons	President	2007
David Stangeland	Vice-President	2007
Patty Fosaaen	Secretary	2005
Revelyn Lonning	Member	2005
Donald Angel	Member	2007
<u>Hospital Officials</u>		
Michael Myers	Administrator	
Scott Knode	Chief Financial Officer	



Consultants • Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

The Board of Trustees
Veterans Memorial Hospital
Waukon, Iowa

We have audited the accompanying balance sheets of **Veterans Memorial Hospital** as of June 30, 2004 and 2003, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America, Chapter 11 of the Code of Iowa, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards and provisions require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of **Veterans Memorial Hospital** as of June 30, 2004 and 2003, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1 to the financial statements, effective July 1, 2003, **Veterans Memorial Hospital** implemented Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*; Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*; and Statement No. 38, *Certain Financial Statement Note Disclosures*. As a result, the Hospital changed its accounting policy related to financial statement presentation to comply with the provisions of GASB Statements No. 34 and No. 37. GASB Statement No. 38 modifies, establishes, and rescinds certain financial statement disclosure requirements.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 29, 2004, on our consideration of **Veterans Memorial Hospital's** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Management's Discussion and Analysis on page 4 and the Budgetary Comparison Information on page 20 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion it.

Side Bailey LLP

Dubuque, Iowa
July 29, 2004

Veterans Memorial Hospital Management's Discussion and Analysis June 30, 2004

This section of Veterans Memorial Hospital's annual financial report presents background information and management's analysis of the financial performance during the fiscal year that ended June 30, 2004. We encourage readers to read this analysis in conjunction with the financial statements in this report.

Financial Highlights – Balance Sheet

- Cash increased by \$315,054 while patient receivables decreased by \$267,683.
- Days of Revenue in patient receivables decreased from 114 days to 96 days.
- A receivable of \$145,000 reflects an estimate of amounts owed at year end by Medicare and Medicaid.
- A total of approximately \$86,000 was spent on property, plant, or equipment during the year.
- Long-term debt was decreased by \$270,000 during the year.

Financial Highlights – Statement of Revenues, Expenses, and Changes in Net Assets

- Gross Patient Service Revenue increased by \$721,893, while Total Operating Revenues increased by only \$394,421.
- 67% of Total Patient Service Revenue was from outpatient services.
- Total inpatient days decreased 2.7% from June 30, 2003, while total outpatient occasions of service increased 3.2%.
- Total Operating Expenses increased by \$640,313, or 8.6%. This increase was larger than our increase in Total Operating Revenues, which caused a significant decrease in overall profitability.

Financial Highlights – Statement of Cash Flows

- Cash and cash equivalents increased from \$158,288 at July 1, 2003 to \$473,342 at June 20, 2004.

There are 11 notes to the financial statements included in the audit report. All of the notes are consistent with and similar to audit reports from prior years. There are also several supplementary schedules that provide the reader detail about the source of the Hospital's revenues and expenses. The reader is encouraged to examine these notes and schedules for additional information.

Factors Bearing on Financial Future

- Two surgeons, a general surgeon and an orthopedic surgeon, started performing procedures at VMH in July 2004. This should increase total surgical volumes in the future.
- Gunderson Clinic is close to finalizing a lease agreement with the City of Waukon. This would allow a medical office building to be built, attached to the Hospital. Gunderson would recruit at least two family practice physicians to Waukon. This should impact future patient volumes at VMH positively.
- Discussions have begun regarding the possibility of VMH building a second operating room suite to accommodate projected future growth in surgical procedures.

Questions regarding the information provided in this report or requests for additional financial information should be addressed to the office of the Chief Financial Officer at the following address:

Veterans Memorial Hospital
40 1st Street S.E.
Waukon, IA 52172

VETERANS MEMORIAL HOSPITAL
BALANCE SHEETS
JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 473,342	\$ 158,288
Assets limited as to use - Note 4	50,540	71,743
Receivables		
Patient, net of estimated uncollectibles of \$780,000 in 2004 and \$727,000 in 2003	2,065,602	2,333,285
Estimated third-party payor settlements	145,000	-
Bequest	25,000	-
Other	9,000	21,136
Supplies	142,460	127,079
Prepaid expenses	<u>40,492</u>	<u>62,365</u>
 Total current assets	 <u>2,951,436</u>	 <u>2,773,896</u>
 ASSETS LIMITED AS TO USE - Note 4		
Investments		
By board for capital improvements and debt retirement	272,996	301,103
Under indenture agreement	<u>50,540</u>	<u>71,743</u>
	323,536	372,846
 Less amount required to meet current obligations	 <u>(50,540)</u>	 <u>(71,743)</u>
 Total assets limited as to use, excluding current portion	 <u>272,996</u>	 <u>301,103</u>
 LAND, BUILDINGS, AND EQUIPMENT, net - Note 5	 <u>6,480,315</u>	 <u>6,864,968</u>
 OTHER ASSETS		
Gift fund investments - Note 4	1,641	1,628
Deferred financing costs, net of accumulated amortization of \$77,914 in 2004 and \$66,845 in 2003	<u>86,570</u>	<u>97,639</u>
 Total other assets	 <u>88,211</u>	 <u>99,267</u>
 Total assets	 <u>\$ 9,792,958</u>	 <u>\$ 10,039,234</u>

See notes to financial statements.

	<u>2004</u>	<u>2003</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current maturities of long-term debt - Note 7	\$ 142,061	\$ 294,347
Accounts payable		
Trade	282,233	324,655
Estimated third-party payor settlements	-	25,000
Accrued expenses		
Salaries and wages	178,764	156,060
Vacation	220,703	203,650
Payroll taxes and other	31,068	26,586
Interest	<u>24,077</u>	<u>26,237</u>
Total current liabilities	878,906	1,056,535
LONG-TERM DEBT, less current maturities - Note 7	<u>2,550,000</u>	<u>2,692,061</u>
Total liabilities	<u>3,428,906</u>	<u>3,748,596</u>
NET ASSETS		
Invested in capital assets, net of related debt	3,788,254	3,878,560
Unrestricted	<u>2,575,798</u>	<u>2,412,078</u>
Total net assets	<u>6,364,052</u>	<u>6,290,638</u>
 Total liabilities and net assets	 <u>\$ 9,792,958</u>	 <u>\$ 10,039,234</u>

VETERANS MEMORIAL HOSPITAL
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
OPERATING REVENUES		
Net patient service revenue (net of provision for bad debts of \$346,065 in 2004 and \$232,386 in 2003) - Notes 2 and 3	\$ 7,833,559	\$ 7,436,888
Other operating revenues	<u>421,907</u>	<u>424,157</u>
TOTAL OPERATING REVENUES	<u>8,255,466</u>	<u>7,861,045</u>
OPERATING EXPENSES		
Salaries and wages	3,488,364	3,172,304
Medical specialist fees	182,911	187,769
Supplies and other expenses	3,948,795	3,614,400
Depreciation and amortization	<u>481,681</u>	<u>486,965</u>
TOTAL OPERATING EXPENSES	<u>8,101,751</u>	<u>7,461,438</u>
INCOME FROM OPERATIONS	<u>153,715</u>	<u>399,607</u>
NONOPERATING REVENUES (EXPENSES)		
Noncapital grants and contributions	37,415	50,375
Investment income	3,761	11,589
Payment of interest on debt	<u>(157,308)</u>	<u>(174,403)</u>
TOTAL NONOPERATING REVENUES (EXPENSES)	<u>(116,132)</u>	<u>(112,439)</u>
REVENUES IN EXCESS OF EXPENSES BEFORE CAPITAL GRANTS AND CONTRIBUTIONS AND TRANSFER	37,583	287,168
Capital grants and contributions	35,831	165,156
Transfer to City of Waukon	<u>-</u>	<u>(20,000)</u>
INCREASE IN NET ASSETS	73,414	432,324
NET ASSETS BEGINNING OF YEAR	<u>6,290,638</u>	<u>5,858,314</u>
NET ASSETS END OF YEAR	<u>\$ 6,364,052</u>	<u>\$ 6,290,638</u>

See notes to financial statements.

VETERANS MEMORIAL HOSPITAL
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts of patient service revenue	\$ 7,931,242	\$ 6,758,880
Other receipts	434,043	455,431
Payments of salaries and wages	(3,446,285)	(3,117,252)
Payments of medical specialist fees	(182,911)	(187,769)
Payments of supplies and other expenses	<u>(3,984,725)</u>	<u>(3,568,636)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>751,364</u>	<u>340,654</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Noncapital grants and contributions received	<u>12,415</u>	<u>50,375</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of property and equipment	(85,959)	(221,968)
Capital grants and contributions received	35,831	165,156
Transfer to City of Waukon	-	(20,000)
Payment of interest on debt	(157,308)	(174,403)
Payment of principal on debt	<u>(294,347)</u>	<u>(296,317)</u>
NET CASH USED FOR CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(501,783)</u>	<u>(547,532)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
(Increase) decrease in fund investments	(13)	201,576
Decrease in assets limited as to use	49,310	45,033
Investment income received	<u>3,761</u>	<u>11,589</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>53,058</u>	<u>258,198</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	315,054	101,695
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>158,288</u>	<u>56,593</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 473,342</u>	<u>\$ 158,288</u>

(continued)

VETERANS MEMORIAL HOSPITAL
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
RECONCILIATION OF INCOME FROM OPERATIONS		
TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Income from operations	\$ 153,715	\$ 399,607
Adjustments to reconcile income from operations to net cash provided by operating activities		
Depreciation and amortization	481,681	486,965
Changes in assets and liabilities		
Receivables	279,819	(276,734)
Supplies	(15,381)	(4,544)
Prepaid expenses	21,873	3,514
Accounts payable	(42,422)	46,794
Estimated third party payor settlements	(170,000)	(370,000)
Accrued expenses	<u>42,079</u>	<u>55,052</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 751,364</u>	<u>\$ 340,654</u>

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Veterans Memorial Hospital (Hospital) is a 25-bed public hospital located in Waukon, Iowa. It is organized under Chapter 392 of the Iowa Code and governed by a five member Board of Trustees elected for alternating terms of four years. The Hospital has been recognized by the Internal Revenue Service as exempt from federal income taxes under Internal Revenue Code Section 501(c)(3).

Reporting Entity

For financial reporting purposes, Veterans Memorial Hospital has included all funds, organizations, agencies, boards, commissions, and authorities. The Hospital has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Hospital are such that exclusion would cause the Hospital's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Hospital to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the Hospital.

Basis of Presentation

Effective July 1, 2003, the Hospital implemented the following new accounting standards issued by the Governmental Accounting Standards Board (GASB): Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*; Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*; and Statement No. 38, *Certain Financial Statement Note Disclosures*. The adoption of these pronouncements had no financial impact on the Hospital.

GASB Statements No. 34 and No. 37 relate to changes in financial statement presentation. Statement 34 established standards for external financial reporting for all state and local governmental entities, which include a balance sheet; a statement of revenues, expenses, and changes in net assets; and a direct method statement of cash flows. It requires the classification of net assets into three components – invested in capital assets, net of related debt, unrestricted, and restricted. These classifications are defined as follows:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- Unrestricted – This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt." Unrestricted net assets often have constraints on resources imposed by management which can be removed or modified. When both restricted and unrestricted resources are available for use, generally it is the Hospital's policy to use restricted resources first.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

- Restricted – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

The adoption of Statement 34 resulted in the previously reported unrestricted fund balance amounts being classified to conform to the above net asset classifications. Additionally, the Hospital restated the 2003 statement of cash flows to conform to the direct method of reporting cash receipts and disbursements.

GASB Statement No. 38 modifies, establishes, and rescinds certain financial statement disclosure requirements.

Basis of Accounting

The Hospital reports in accordance with accounting principles generally accepted in the United States of America as specified by the American Institute of Certified Public Accountants' *Audits of Providers of Health Care Services* and, as a governmental entity, also provides certain disclosures required by the Governmental Accounting Standards Board (GASB). Revenues are recognized when earned and expenses are recorded when the liability is incurred.

In reporting its financial activity, the Hospital applies all applicable GASB pronouncements for proprietary funds as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with an original maturity of three months or less, excluding assets limited as to use and gift fund investments.

Patient Receivables

Patient receivables are uncollateralized customer and third-party payor obligations. Unpaid patient receivables are not charged interest on amounts owed.

Payments of patient receivables are allocated to the specific claims identified on the remittance advice or, if unspecified, are applied to the earliest unpaid claim.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

The carrying amount of patient receivables is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected from patients and third-party payors. Management reviews patient receivables by payor class and applies percentages to determine estimated amounts that will not be collected from third parties under contractual agreements and amounts that will not be collected from patients due to bad debts. Management considers historical write off and recovery information in determining the estimated bad debt provision. Management also reviews accounts to determine if classification as charity care is appropriate.

Supplies

Supplies are stated at lower of average cost or market.

Assets Limited as to Use

Assets limited as to use include assets set aside by the Board of Trustees for future capital improvements and debt retirement, over which the Board retains control and may, at its discretion, subsequently use for other purposes; and assets held by trustees under an indenture agreement. Assets limited as to use that are available for obligations classified as current liabilities are reported in current assets.

Land, Buildings, and Equipment

Land, buildings, and equipment acquisitions in excess of \$1,000 are capitalized and recorded at cost. Land, buildings, and equipment donated for Hospital operations are recorded as additions to net assets at fair value at the date of receipt. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Amortization is included in depreciation and amortization in the financial statements. Interest expense related to construction projects is capitalized.

The estimated useful lives of property and equipment are as follows:

Land improvements	5-15 years
Buildings and improvements	5-40 years
Equipment	5-20 years

Advertising Costs

Costs incurred for producing and distributing advertising are expensed as incurred. The Hospital incurred \$27,780 and \$20,911 for advertising costs in 2004 and 2003, respectively.

Deferred Financing Costs

Deferred financing costs are amortized over the period the related obligation is outstanding using the effective interest method.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

Compensated Absences

Hospital employees accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, death, or retirement. The cost of vacation is recorded as a current liability on the balance sheet. The compensated absences liability has been computed based on rates of pay in effect at June 30, 2004.

Net Assets

Net assets of the Hospital are classified in three components. *Net assets invested in capital assets, net of related debt* consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted net assets* are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital. *Unrestricted net assets* are remaining net assets that do not meet the definition of *invested in capital assets, net of related debt* or *restricted*.

Operating Revenues and Expenses

The Hospital's statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Hospital's principal activity. Nonexchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Net Patient Service Revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates, reimbursed costs, discounted charges, and per diem payments. Patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity Care

To fulfill its mission of community service, the Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Revenue from services to these patients is automatically recorded in the accounting system at the established rates, but the Hospital does not pursue collection of the amounts. The resulting adjustments are recorded as adjustments to patient service revenue depending on the timing of the charity determination.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

Grants and Contributions

Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenue. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

Restricted Resources

When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources.

Reclassifications

Certain prior period amounts within the accompanying statements have been reclassified for comparability.

Other Significant Accounting Policies

Other significant accounting policies are set forth in the financial statements and the notes thereto.

NOTE 2 – CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. The amounts of charges foregone for services and supplies furnished under its charity care policy during the years ended June 30, 2004 and 2003, were \$118,969 and \$129,927, respectively.

NOTE 3 – NET PATIENT SERVICE REVENUE

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare: The Hospital is licensed as a Critical Access Hospital (CAH). The Hospital is reimbursed for most inpatient and outpatient services at cost with final settlement determined after submission of annual cost reports by the Hospital and are subject to audits thereof by the Medicare fiscal intermediary. The Hospital's Medicare cost reports have been settled by the Medicare fiscal intermediary through the period ended June 30, 2001. The Hospital's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Hospital.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
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Medicaid: Inpatient and outpatient services rendered to Medicaid program beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicaid fiscal intermediary. The Hospital's Medicaid cost reports have been settled by the Medicaid fiscal intermediary through June 30, 2001.

The Hospital has also entered into payment agreements with certain commercial insurance carriers and other organizations. The basis for payment to the Hospital under these agreements may include prospectively determined rates and discounts from established charges.

Laws and regulations governing the Medicare, Medicaid, and other programs are extremely complex and subject to interpretation.

A summary of net patient service revenue and contractual adjustments for the years ended June 30, 2004 and 2003, is as follows:

	2004	2003
Total patient service revenue	\$ 10,445,378	\$ 9,723,485
Contractual adjustments		
Medicare	(1,578,468)	(1,680,061)
Medicaid	(186,962)	(85,617)
Blue Cross	(245,957)	(105,871)
Other	(254,367)	(182,662)
Total contractual adjustments	(2,265,754)	(2,054,211)
Net patient service revenue	8,179,624	7,669,274
Provision for bad debts	(346,065)	(232,386)
Net patient service revenue (net of provision for bad debts)	\$ 7,833,559	\$ 7,436,888

NOTE 4 – CASH AND DEPOSITS

The Hospital's deposits in banks at June 30, 2004 and 2003, were entirely covered by federal depository insurance or the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Hospital is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts, and warrants or improvement certificates of a drainage district.

Investments reported are not subject to risk categorization. Money market accounts classified as investments in the financial statements are presented as cash and deposits in this note.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

At June 30, 2004 and 2003, the Hospital's carrying amounts of cash and deposits are as follows:

	<u>2004</u>	<u>2003</u>
Money market accounts	\$ <u>325,177</u>	\$ <u>374,474</u>

NOTE 5 – LAND, BUILDINGS, AND EQUIPMENT

A summary of land, buildings, and equipment at June 30, 2004 and 2003, follows:

	<u>June 30, 2003</u>			<u>June 30, 2004</u>
	<u>Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance</u>
Cost				
Land	\$ 299,281	\$ -	\$ -	\$ 299,281
Land improvements	125,398	-	-	125,398
Buildings and leasehold improvements	7,962,467	7,430	-	7,969,897
Equipment	<u>2,556,165</u>	<u>78,529</u>	<u>-</u>	<u>2,634,694</u>
	<u>\$ 10,943,311</u>	<u>\$ 85,959</u>	<u>\$ -</u>	<u>\$ 11,029,270</u>
Accumulated depreciation				
Land improvements	\$ 68,202	\$ 8,438	\$ -	\$ 76,640
Buildings and leasehold improvements	2,085,422	308,970	-	2,394,392
Equipment	<u>1,924,719</u>	<u>153,204</u>	<u>-</u>	<u>2,077,923</u>
	<u>\$ 4,078,343</u>	<u>\$ 470,612</u>	<u>\$ -</u>	<u>\$ 4,548,955</u>
	<u>June 30, 2002</u>			<u>June 30, 2003</u>
	<u>Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance</u>
Cost				
Land	\$ 286,197	\$ 13,084	\$ -	\$ 299,281
Land improvements	124,301	1,097	-	125,398
Buildings and leasehold improvements	7,913,625	48,842	-	7,962,467
Equipment	<u>2,397,220</u>	<u>158,945</u>	<u>-</u>	<u>2,556,165</u>
	<u>\$ 10,721,343</u>	<u>\$ 221,968</u>	<u>\$ -</u>	<u>\$ 10,943,311</u>
Accumulated depreciation				
Land improvements	\$ 59,757	\$ 8,445	\$ -	\$ 68,202
Buildings and leasehold improvements	1,773,451	311,971	-	2,085,422
Equipment	<u>1,769,355</u>	<u>155,364</u>	<u>-</u>	<u>1,924,719</u>
	<u>\$ 3,602,563</u>	<u>\$ 475,780</u>	<u>\$ -</u>	<u>\$ 4,078,343</u>

(continued on next page)

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

NOTE 6 – LEASES

The Hospital leases certain equipment under noncancellable long-term lease agreements. Certain leases have been recorded as capitalized leases and others as operating leases. Total equipment and building rental expense for all operating leases for the years ended June 30, 2004 and 2003, was \$86,076 and \$58,944, respectively. The capitalized leased assets consist of:

	<u>2004</u>	<u>2003</u>
Equipment	\$ 112,235	\$ 112,235
Less accumulated amortization (included as depreciation and amortization on the accompanying financial statements)	<u>(101,012)</u>	<u>(78,565)</u>
	<u>\$ 11,223</u>	<u>\$ 33,670</u>

Minimum future lease payments for the capital leases are as follows:

<u>Year Ending June 30,</u>	
2005	\$ 7,234
Less interest	<u>(173)</u>
Present value of minimum lease payments – Note 7	<u>\$ 7,061</u>

NOTE 7 – LONG-TERM DEBT

Long-term debt consists of:

	<u>June 30 2003 Balance</u>	<u>Additions</u>	<u>Payments</u>	<u>June 30 2004 Balance</u>	<u>Amounts Due Within One Year</u>
1998 revenue bonds, 4.25% to 5.60%, principal maturing in varying annual amounts to May, 2018, collateralized by a pledge of the Hospital's net revenues	\$ 2,955,000	\$ -	\$ 270,000	\$ 2,685,000	\$ 135,000
Capitalized lease obligations – Note 6	<u>31,408</u>	<u>-</u>	<u>24,347</u>	<u>7,061</u>	<u>7,061</u>
	<u>\$ 2,986,408</u>	<u>\$ -</u>	<u>\$ 294,347</u>	<u>2,692,061</u>	<u>\$ 142,061</u>
Less current maturities				<u>(142,061)</u>	
Long-term debt, less current maturities				<u>\$ 2,550,000</u>	

(continued on next page)

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

Long-term debt requirements to maturities are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 142,061	\$ 144,636	\$ 286,697
2006	140,000	137,848	277,848
2007	150,000	130,917	280,917
2008	155,000	123,418	278,418
2009	165,000	115,590	280,590
Thereafter	<u>1,940,000</u>	<u>578,953</u>	<u>2,518,953</u>
	<u>\$ 2,692,061</u>	<u>\$ 1,231,362</u>	<u>\$ 3,923,423</u>

	<u>June 30 2002 Balance</u>	<u>Additions</u>	<u>Payments</u>	<u>June 30 2003 Balance</u>	<u>Amounts Due Within One Year</u>
1998 revenue bonds, 4.25% to 5.60%, principal maturing in varying annual amounts to May, 2018, collateralized by a pledge of the Hospital's net revenues	\$ 3,215,000	\$ -	\$ 260,000	\$ 2,955,000	\$ 270,000
Contract payable, 8%, due in monthly payments of \$532 including interest	8,052	-	8,052	-	-
Capitalized lease obligations	<u>59,673</u>	<u>-</u>	<u>28,265</u>	<u>31,408</u>	<u>24,347</u>
	<u>\$ 3,282,725</u>	<u>\$ -</u>	<u>\$ 296,317</u>	<u>2,986,408</u>	<u>\$ 294,347</u>
Less current maturities				<u>(294,347)</u>	
Long-term debt, less current maturities				<u>\$ 2,692,061</u>	

NOTE 8 – PENSION AND RETIREMENT BENEFITS

The Hospital contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

VETERANS MEMORIAL HOSPITAL
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2004 AND 2003

Plan members are required to contribute 3.70% of their annual covered salary and the Hospital is required to contribute 5.75% of annual covered payroll for the years ended June 30, 2004, 2003, and 2002. Contribution requirements are established by state statute. The Hospital's contributions to IPERS for the years ended June 30, 2004, 2003, and 2002, were \$199,494, \$180,930, and \$156,301, respectively, equal to the required contributions for each year.

NOTE 9 – MALPRACTICE INSURANCE

The Hospital has malpractice insurance coverage to provide protection for professional liability losses on a claims-made basis subject to a limit of \$1 million per claim and an annual aggregate limit of \$3 million. Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on occurrences during its term, but reported subsequently, will be uninsured.

NOTE 10 – RISK MANAGEMENT

The Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. These risks are covered by commercial insurance purchased from independent third parties. The Hospital assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

NOTE 11 – CONCENTRATION OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. The mix of receivables from third-party payors and patients at June 30, 2004 and 2003, was as follows:

	<u>2004</u>	<u>2003</u>
Medicare	47%	41%
Medicaid	7	5
Commercial insurance	24	32
Other third-party payors and patients	<u>22</u>	<u>22</u>
	<u>100%</u>	<u>100%</u>



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**INDEPENDENT AUDITOR'S REPORT ON
SUPPLEMENTARY INFORMATION**

The Board of Trustees
Veterans Memorial Hospital
Waukon, Iowa

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Eide Bailly LLP

Dubuque, Iowa
July 29, 2004

VETERANS MEMORIAL HOSPITAL**BUDGETARY COMPARISON SCHEDULE OF REVENUES, EXPENSES, AND CHANGES IN
NET ASSETS – BUDGET AND ACTUAL (ACCRUAL BASIS)
YEARS ENDED JUNE 30, 2004 AND 2003**

	Accrual Basis	Budget	Variance Favorable (Unfavorable)
Estimated amount to be raised by taxation	\$ 9,000	\$ 9,000	\$ -
Estimated other revenues	<u>8,323,473</u>	<u>8,955,000</u>	<u>(631,527)</u>
	8,332,473	8,964,000	(631,527)
Expenses	<u>8,259,059</u>	<u>8,464,000</u>	<u>204,941</u>
Net	73,414	500,000	<u>\$ (426,586)</u>
Balance beginning of year	<u>6,290,638</u>	<u>5,898,439</u>	
Balance end of year	<u>\$ 6,364,052</u>	<u>\$ 6,398,439</u>	

The Board of Trustees annually prepares and adopts a budget designating the amount necessary for the improvement and maintenance of the Hospital on the accrual basis following required public notice and hearing in accordance with Chapters 24 and 347 of the Code of Iowa. The Board of Trustees certifies the approved budget to the appropriate county auditors. The budget may be amended during the year utilizing similar statutorily prescribed procedures. Formal and legal budgetary control is based on total expenditures.

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF NET PATIENT SERVICE REVENUE
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
PATIENT SERVICE REVENUE		
Routine Services		
Adults and pediatrics	\$ 823,830	\$ 802,445
Nursery	64,800	54,390
Skilled care	140,980	139,840
Intermediate care	240	300
Respite	1,800	1,440
Hospice	14,760	13,560
Observation	266,482	275,912
Same day surgery	69,782	73,510
Operating and recovery rooms	765,533	914,757
Delivery and labor rooms	80,170	54,786
Central services and supply	723,768	508,985
Intravenous solutions	279,007	269,193
Emergency services	417,984	356,868
Laboratory	1,173,164	1,048,798
Radiology	1,577,639	1,520,001
Electrocardiology	106,917	123,955
Pharmacy	1,413,176	1,166,465
Anesthesiology	450,348	498,875
Respiratory therapy	86,732	131,643
Physical therapy	804,316	821,136
Occupational therapy	162,494	192,029
Speech therapy	17,364	27,040
Cardiac rehabilitation	164,250	129,495
Chemotherapy	25,682	15,593
Ambulance service	159,780	101,512
Community and home care	770,536	607,036
Nutrition instruction	2,813	3,848
	<u>10,564,347</u>	<u>9,853,412</u>
Charity care	<u>(118,969)</u>	<u>(129,927)</u>
	<u>10,445,378</u>	<u>9,723,485</u>
 Total patient service revenue*	 <u>10,445,378</u>	 <u>9,723,485</u>
 *TOTAL PATIENT SERVICE REVENUE - RECLASSIFIED		
Inpatient revenue	3,584,255	3,615,887
Outpatient revenue	6,980,092	6,237,525
Charity care	<u>(118,969)</u>	<u>(129,927)</u>
	<u>10,445,378</u>	<u>9,723,485</u>

(continued)

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF NET PATIENT SERVICE REVENUE
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
CONTRACTUAL ADJUSTMENTS		
Medicare	\$ (1,578,468)	\$ (1,680,061)
Medicaid	(186,962)	(85,617)
Blue Cross	(245,957)	(105,871)
Other	<u>(254,367)</u>	<u>(182,662)</u>
Total contractual adjustments	<u>(2,265,754)</u>	<u>(2,054,211)</u>
NET PATIENT SERVICE REVENUE	8,179,624	7,669,274
PROVISION FOR BAD DEBTS	<u>(346,065)</u>	<u>(232,386)</u>
NET PATIENT SERVICE REVENUE (NET OF PROVISION FOR BAD DEBTS)	<u>\$ 7,833,559</u>	<u>\$ 7,436,888</u>

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF OTHER OPERATING REVENUES
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
OTHER OPERATING REVENUES		
County reimbursement - Community and Home Care	\$ 100,000	\$ 100,000
Rental - net of direct expenses	76,825	80,208
Community and Home Care Clinics, etc.	67,907	67,275
Grants	46,211	10,235
Housekeeping	32,143	33,249
Frozen Meals	-	32,979
Contract physical therapy	23,177	32,952
Healthy Lifestyle Center	25,828	28,747
City tax	9,000	9,000
Cafeteria	8,977	7,488
Workshops, clinics, etc.	6,855	6,426
Gifts for operations	6,748	2,300
Medical records copies	1,574	1,702
Laundry	971	1,392
Vending machines	1,085	766
Other	<u>14,606</u>	<u>9,438</u>
TOTAL OTHER OPERATING REVENUES	<u>\$ 421,907</u>	<u>\$ 424,157</u>

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF EXPENSES
YEARS ENDED JUNE 30, 2004 AND 2003

	2004	2003
NURSING ADMINISTRATION		
Salaries and wages	\$ 64,901	\$ 62,434
Supplies and other expenses	48,309	7,502
	<u>113,210</u>	<u>69,936</u>
ROUTINE SERVICES		
Salaries and wages	947,178	892,867
Supplies and other expenses	61,293	59,478
	<u>1,008,471</u>	<u>952,345</u>
OPERATING AND RECOVERY ROOMS		
Salaries and wages	168,389	124,511
Supplies and other expenses	125,236	218,707
	<u>293,625</u>	<u>343,218</u>
DELIVERY AND LABOR ROOMS		
Salaries and wages	12,274	10,456
Supplies and other expenses	-	782
	<u>12,274</u>	<u>11,238</u>
CENTRAL SERVICES AND SUPPLY		
Salaries and wages	26,487	22,311
Supplies and other expenses	218,299	102,641
	<u>244,786</u>	<u>124,952</u>
EMERGENCY SERVICES		
Salaries and wages	91,874	77,363
Medical specialist fees	158,711	152,280
Supplies and other expenses	6,365	5,938
	<u>256,950</u>	<u>235,581</u>
LABORATORY		
Salaries and wages	175,050	155,719
Medical specialist fees	24,200	24,200
Supplies and other expenses	248,273	243,061
	<u>447,523</u>	<u>422,980</u>
RADIOLOGY		
Salaries and wages	172,515	168,371
Professional fees	385,987	415,420
Supplies and other expenses	106,290	74,565
	<u>664,792</u>	<u>658,356</u>

(continued)

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF EXPENSES
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
ELECTROCARDIOLOGY		
Salaries and wages	\$ 2,044	\$ 1,652
Medical specialist fees	-	11,289
Supplies and other expenses	<u>859</u>	<u>955</u>
	<u>2,903</u>	<u>13,896</u>
 PHARMACY		
Drugs	429,421	336,553
Supplies and other expenses	<u>84,479</u>	<u>75,454</u>
	<u>513,900</u>	<u>412,007</u>
 ANESTHESIOLOGY		
Salaries and wages	109,090	103,893
Supplies and other expenses	<u>57,165</u>	<u>46,499</u>
	<u>166,255</u>	<u>150,392</u>
 RESPIRATORY THERAPY		
Salaries and wages	80,085	76,187
Supplies and other expenses	<u>767</u>	<u>1,362</u>
	<u>80,852</u>	<u>77,549</u>
 PHYSICAL THERAPY		
Salaries and wages	86,372	77,026
Supplies and other expenses	<u>267,969</u>	<u>266,674</u>
	<u>354,341</u>	<u>343,700</u>
 OCCUPATIONAL THERAPY		
Supplies and other expenses	<u>114,559</u>	<u>120,081</u>
 SPEECH THERAPY		
Supplies and other expenses	<u>8,346</u>	<u>19,879</u>
 CARDIAC REHABILITATION		
Salaries and wages	32,027	27,848
Supplies and other expenses	<u>5,793</u>	<u>5,229</u>
	<u>37,820</u>	<u>33,077</u>

(continued)

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF EXPENSES
YEARS ENDED JUNE 30, 2004 AND 2003

	2004	2003
CHEMOTHERAPY		
Salaries and wages	\$ 10,812	\$ 6,991
Supplies and other expenses	765	661
	<u>11,577</u>	<u>7,652</u>
AMBULANCE SERVICE		
Salaries and wages	65,844	61,962
Supplies and other expenses	8,805	4,644
	<u>74,649</u>	<u>66,606</u>
COMMUNITY AND HOME CARE		
Salaries and wages	415,776	343,292
Supplies and other expenses	94,090	87,377
	<u>509,866</u>	<u>430,669</u>
NUTRITION INSTRUCTION		
Salaries and wages	4,507	1,611
Supplies and other expenses	92	3,646
	<u>4,599</u>	<u>5,257</u>
MEDICAL RECORDS		
Salaries and wages	92,673	90,369
Supplies and other expenses	11,263	11,215
	<u>103,936</u>	<u>101,584</u>
DIETARY		
Salaries and wages	163,518	156,154
Food	29,981	41,648
Supplies and other expenses	16,231	23,254
	<u>209,730</u>	<u>221,056</u>
PLANT OPERATION AND MAINTENANCE		
Salaries and wages	105,522	106,386
Utilities	100,046	88,978
Supplies and other expenses	67,240	56,871
	<u>272,808</u>	<u>252,235</u>

(continued)

VETERANS MEMORIAL HOSPITAL
SCHEDULES OF EXPENSES
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
HOUSEKEEPING		
Salaries and wages	\$ 184,659	\$ 176,053
Supplies and other expenses	<u>17,343</u>	<u>15,969</u>
	<u>202,002</u>	<u>192,022</u>
LAUNDRY AND LINEN		
Salaries and wages	29,759	27,561
Supplies and other expenses	<u>12,420</u>	<u>13,777</u>
	<u>42,179</u>	<u>41,338</u>
ADMINISTRATIVE SERVICES		
Salaries and wages	447,008	401,287
Auditing and accounting fees	27,000	45,704
Collection fees	30,626	22,032
Telephone	28,237	27,071
Supplies and other expenses	<u>263,373</u>	<u>230,291</u>
	<u>796,244</u>	<u>726,385</u>
UNASSIGNED EXPENSES		
Depreciation	470,612	475,780
Amortization	11,069	11,185
Insurance	51,224	48,838
Employee benefits		
FICA	247,399	225,973
IPERS	199,493	180,930
Group health insurance	496,171	419,067
Workers' compensation insurance	34,943	29,993
Other	<u>42,643</u>	<u>35,681</u>
	<u>1,553,554</u>	<u>1,427,447</u>
TOTAL EXPENSES	<u>\$ 8,101,751</u>	<u>\$ 7,461,438</u>

VETERANS MEMORIAL HOSPITAL
PATIENT RECEIVABLES AND ALLOWANCE FOR DOUBTFUL ACCOUNTS
JUNE 30, 2004 AND 2003

ANALYSIS OF AGING

	<u>June 30, 2004</u>		<u>June 30, 2003</u>	
	<u>Amount</u>	<u>Percent to Total</u>	<u>Amount</u>	<u>Percent to Total</u>
DAYS SINCE DISCHARGE				
0 to 30 days	\$ 945,880	33.24%	\$ 897,987	29.34%
1 to 2 months	583,547	20.51	610,621	19.95
2 to 3 months	334,990	11.78	335,848	10.97
3 to 6 months	462,817	16.26	452,668	14.79
6 to 12 months	333,039	11.70	518,816	16.95
Over 1 year	<u>185,329</u>	<u>6.51</u>	<u>244,345</u>	<u>8.00</u>
	2,845,602	<u>100.00%</u>	3,060,285	<u>100.00%</u>
Less: Allowance for doubtful accounts	320,000		252,000	
Allowance for contractual adjustments	<u>460,000</u>		<u>475,000</u>	
Net	<u>\$ 2,065,602</u>		<u>\$ 2,333,285</u>	

ALLOWANCE FOR DOUBTFUL ACCOUNTS
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
BALANCE, BEGINNING OF YEAR	\$ 252,000	\$ 215,000
Add: Provision for bad debts	346,065	232,386
Recoveries of accounts written off	105,373	60,590
Less: Accounts written off	<u>(383,438)</u>	<u>(255,976)</u>
BALANCE, END OF YEAR	<u>\$ 320,000</u>	<u>\$ 252,000</u>

VETERANS MEMORIAL HOSPITAL
SUPPLIES/PREPAID EXPENSES
JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
SUPPLIES		
Central stores	\$ 47,279	\$ 43,921
Pharmacy	61,912	50,550
Physical therapy	3,813	2,596
Suture	4,485	4,890
Radiology	4,188	6,208
Laboratory	18,594	16,039
Anesthesiology	<u>2,189</u>	<u>2,875</u>
Total supplies	<u>\$ 142,460</u>	<u>\$ 127,079</u>
PREPAID EXPENSES		
Pension	\$ 10,835	\$ 23,483
Insurance	11,008	13,743
Maintenance contracts	15,261	21,975
Dues	<u>3,388</u>	<u>3,164</u>
Total prepaid expenses	<u>\$ 40,492</u>	<u>\$ 62,365</u>

VETERANS MEMORIAL HOSPITAL
SCHEDULE OF INSURANCE IN FORCE AT JUNE 30, 2004

<u>Company and Policy Number</u>	<u>Description</u>	<u>Amount of Coverage</u>	<u>Annual Premium</u>	<u>Expiration Date</u>
Cincinnati Insurance Co. CAP 549 06 55	Building and contents Blanket earnings and expense Auto liability	\$ 12,007,559 \$ 1,174,484 \$ 1,000,000	\$ 11,771	12/2/04
PIC Wisconsin #130301	Professional and premises liability	\$ 1,000,000/ 3,000,000	\$ 33,031	12/2/04
PIC Wisconsin #130302	General liability	\$ 1,000,000		
PIC Wisconsin #130303	Umbrella excess liability	\$ 2,000,000		
Farm Bureau Mutual Insurance Co. #17805	Workers' compensation	\$ 500,000	\$ 42,175	4/1/05
Fireman's Fund Insurance Co. #NDP-000-8552-8271	Directors' and officers' liability	\$ 1,000,000	\$ 5,602	3/4/05

VETERANS MEMORIAL HOSPITAL
STATISTICAL INFORMATION
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
PATIENT DAYS		
Acute		
Adults and pediatrics	1,594	1,680
Newborn	161	148
Swing-bed		
Skilled	742	739
Intermediate	3	3
Respite	8	14
NUMBER OF BEDS	25	25
PERCENT OF OCCUPANCY (excluding newborn)	26%	27%
DISCHARGES		
Acute	669	641
Swing-bed	91	91
AVERAGE LENGTH OF STAY		
Acute	2.38	2.62
Swing-bed	8.27	8.31
MOST RECENT YEAR END ROUTINE SERVICE RATES		
Acute		
Private rooms	\$ 495.00	\$ 465.00
2-bed rooms	470.00	440.00
Nursery	400.00	370.00
Skilled care	190.00	190.00
COLLECTION STATISTICS		
Net accounts receivable – patients	\$ 2,065,602	\$ 2,333,285
Number of days charges outstanding (1)	96	114
Uncollectible accounts (2)	\$ 495,661	\$ 384,345
Percentage of uncollectible accounts to total charges	4.7%	3.9%

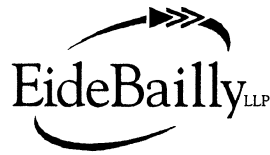
(1) Based on average daily net patient service revenue for April, May, and June.

(2) Includes provision for bad debts, charity care, and collection fees.

VETERANS MEMORIAL HOSPITAL
ANALYSIS OF SINKING FUND
YEARS ENDED JUNE 30, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
Balance, beginning of year	\$ 71,743	\$ 71,628
Add: Deposits	352,800	488,409
Less: Withdrawals	<u>(374,003)</u>	<u>(488,294)</u>
Balance, end of year	<u>\$ 50,540</u>	<u>\$ 71,743</u>

The Hospital is required to maintain a Sinking Fund under the requirements of its Series 1998 Hospital Revenue Bonds Agreement. The Sinking Fund is required to have sufficient deposits to cover the next principal and interest amounts coming due. The Hospital has sufficiently funded this requirement.



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REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Board of Trustees
Veterans Memorial Hospital
Waukon, Iowa

We have audited the accompanying balance sheets of **Veterans Memorial Hospital** as of June 30, 2004 and 2003, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended and have issued our report thereon dated July 29, 2004. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, Chapter 11 of the Code of Iowa, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether **Veterans Memorial Hospital's** financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly we do not express such an opinion. The results of our tests disclosed no instances of non-compliance that are required to be reported under *Government Auditing Standards*. However, we noted a certain immaterial instance of non-compliance that is described in Part II of the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the Hospital's operations for the year ended June 30, 2004, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Hospital. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes. Prior year statutory comments have been resolved except for item II-E-04.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered **Veterans Memorial Hospital's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect **Veterans Memorial Hospital's** ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in Part I as item I-A-04 in the accompanying Schedule of Findings.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We also noted other matters involving the Hospital's operations that we have reported to management in a separate letter dated July 29, 2004. However, we believe the reportable condition described above is not a material weakness. Prior year reportable condition item I-A-04 has not been resolved.

This report, a public record by law, is intended solely for the information and use of the officials, employees, and constituents of **Veterans Memorial Hospital** and other parties to whom **Veterans Memorial Hospital** may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of **Veterans Memorial Hospital** during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Eric Bailey LLP

Dubuque, Iowa
July 29, 2004

VETERANS MEMORIAL HOSPITAL
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2004

Part I: Findings Related to the Financial Statements:

REPORTABLE CONDITION:

I-A-04 Segregation of Duties – One important aspect of internal controls is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The limited number of office personnel prevents a proper segregation of accounting functions necessary to assure optimal internal control.

Recommendation – We realize that with a limited number of office employees, segregation of duties is difficult. However, the Hospital should review its control procedures to obtain the maximum internal control possible under the circumstances.

Response – We are aware of the situation and will continually review the assignment of duties to obtain the maximum internal control possible under the circumstances.

Conclusion – Response accepted.

Part II: Other Findings Related to Required Statutory Reporting:

II-A-04 Official Depositories – A resolution naming official depositories has been adopted by the Board. The maximum deposit amounts stated in the resolution were not exceeded during the year ended June 30, 2004.

II-B-04 Certified Budget – Hospital expenditures during the year ended June 30, 2004, did not exceed amounts budgeted.

II-C-04 Questionable Expenditures – We noted no expenditures that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

II-D-04 Travel Expense – No expenditures of Hospital money for travel expenses of spouses of Hospital officials and/or employees were noted.

II-E-04 Business Transactions – Business transactions between the Hospital and Hospital officials and/or employees are detailed as follows:

<u>Name, Title, and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Northern Aire Rental, company owned by Hospital's purchasing manager	Expense recovery	\$ 35,828

II-F-04 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

II-G-04 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of the Code of Iowa and the Hospital's investment policy were noted.